

# NORTHWESTERN Banker Newsletter

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May 17, 1976

## "Banking Enters Period of Consolidation"

The American banking system has now entered into a period of consolidation, according to Henry Kaufman, general partner and member of the executive committee of Salomon Brothers, international investment banking, market making and research firm.

Mr. Kaufman said that there are definite limits to commercial banking expansion which had been dependent in the past mainly on the inflationary component in Gross National Product and a carving out of a larger share of the intermediation market. The intermediation market is comprised of those financial institutions which receive funds from the public and then reinvest or relend the funds to others. Commercial banks dominate the intermediation market. At the end of 1975, they held \$744 billion in assets, or 43% of all assets held by financial intermediaries.

Mr. Kaufman warned against the United States following the example of some foreign nations in politicizing the banking system.

### Credit Allocation

"The movement to politicize the banks should be well understood if it is to be arrested in time," Mr. Kaufman said. Governmental efforts here could include credit allocation schemes and perhaps

intervention in the lending and investing process through controls over bank management.

He noted that attempts to politicize banking are likely to occur under conditions of high utilization of real resources and high inflation.

"Unfortunately," he remarked, "this process is well underway in many parts of the world where banks have become the servants of off-profligate national policies.

"It is shocking to see," Mr. Kaufman added, "the many loans these banks are forced to make to finance businesses and projects that are losing vast sums of money under the guise of governmental efforts to maintain employment.

"As a consequence, these banks have not only limited freedom of choice but their real liquidity and asset quality deteriorate."

In the United States, he said, the danger to banking and the economy could arise if the government sought to mitigate the disciplines that would be exerted by financial institutions on the economy during future bouts with inflation.

### Equity Capital

Mr. Kaufman noted that banks should not be as hesitant as in the past to increase equity capital. "If the trend in bank capital ratios should persist and capital continues to become a smaller proportion of

total assets, then I believe the politicizing of banks cannot be avoided. I find it difficult to conceive that an enlightened banking industry would risk such a development."

In reviewing the enormous expansion of commercial banking in the 1960s, Mr. Kaufman pointed to three factors which were the basis for the new concept of liability management—the negotiable certificate of deposit, the floating loan rate which removed market risks from bank lending, and the bank holding company.

Tracing the increasing growth of commercial banks, he stated that in the 1950s bank credit growth was a half percentage point less than GNP increases. Then, in the 1960s bank credit grew by 1.6 percentage points more than GNP, and by 1.9 percentage points so far in the 1970s. But, he noted that in 1975, for the first time in two decades, the increase in bank credit in the initial period of an economic recovery did not exceed GNP, a trend which continues in 1976.

The current economic and credit market structures cannot sustain another period of high inflation, Mr. Kaufman stated. If banking credit continues to parallel growth rates in GNP, then it should moderate as GNP growth slows.

**BANKING SYSTEM . . . . .**  
[Turn to page 5, please]

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## Iowa News

The Iowa Senate approved a bill authorizing financial institutions to operate electronic facilities in retail stores last week. The bill, as passed earlier in the House, would allow banks to shift from a year of experimentation to broad use of electronic outlets providing credit to card-carrying customers. The measure was approved 41-2 and now returns to the House for action on three Senate changes. 1. Make banks, savings and loans and credit unions responsible for correcting errors and explaining mixups to customers, 2. to require receipts for all transactions and quarterly

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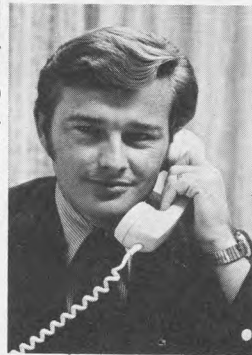


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reports showing what customers spend or borrow in using the machines, and 3. require financial institutions to disclose in advance their terms and fees for the services to customers under the system.

The Senate rejected 20-11 a proposal that would have permitted banks to expand their electronic outlets beyond the metropolitan areas where they are now located.

The five remaining group meetings of the Iowa Bankers Association are being held this week as follows:

17—Gp. 5, Council Bluffs, Ramada Inn.

18—Gp. 6, Des Moines Golf & Country Club.

19—Gp. 7, Waterloo, Conway Civic Center.

20—Gp. 3, Clear Lake, Surf Convention & Civic Center.

21—Gp. 12, Okoboji, New Inn.

Programs for the meetings are published in the May Northwestern Banker. The story for Group 3 incorrectly identified the group officers. They are Don W. Heineking, president, Security State Bank, Hubbard, chairman, and Glenn O. Emmons, executive vice president, Northwood State Bank, secretary. In addition to the association speakers, the two guest

speakers will be Paul R. Giel, director of athletics, University of Minnesota, whose topic is "The Buck Stops Here," and Timothy Hayes, Mayor of Whoopup, N. J., whose topic is "Marriage, Middle Age & Other Perils."

DES MOINES: Tee-off time for Group 6 golfers on Tuesday, May 18, at the Des Moines Golf and Country Club will be between noon and 2:30 p.m., according to Eddie Wolf, vice president, Central National Bank & Trust Company, and golf chairman. (Tuesday morning is ladies' day at the club.)

DES MOINES: Brenton Banks, Inc., has announced the following three new directors: James H. Crane, president, Palo Alto County State Bank, Emmetsburg; George Mechem, president, Brenton Bank and Trust Company, Clarion, and Betty L. Steele, vice president and corporate secretary, Brenton Banks, Inc. Also announced was the promotion of Jerry R. Thornton to assistant vice president-director of marketing for the 17 Brenton banks and affiliate companies.

DUBUQUE: Dubuque Bank & Trust Co.'s application for permission to establish a bank office in Asbury has been denied.

ELKADER: Central State Bank has increased its surplus capital account to \$1 million by a \$200,000 transfer from the undivided profits account.

MARSHALLTOWN: The telephone number for Security Savings Bank has been changed to 515/754-5500.

MASON CITY: American State Bank has received consent to establish a branch at 1610 South Federal Street here.

SHELDON: A merger has been announced whereby Sheldon Federal S & L will merge into First

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His works can be found in private collections in the United States, Canada and England, and have been offered in galleries in New York and Washington, D.C. Two of his paintings have won honors, having been selected in competition for the 1974 Iowa Duck Stamp and the 1975 Iowa Trout Stamp.

Jim is a frequent contributor to the state magazine "Iowa Conservationist" and his works have been featured as covers for the "New York Conservationist" and the "Pennsylvania Game News."




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WELLSBURG: Peoples Savings Bank has announced the following officer changes: R. W. Aikes, chairman; Leland D. Luwe, president; Bernerd J. Harms, vice president and cashier; Norman Homeyer, manager, Cleves office, and Michael A. Nederhoff, assistant cashier.

### Nebraska News

The Nebraska Bankers Association annual Washington, D.C., visit will be held Sunday, June 6, through Tuesday, June 8.

GENEVA: Timothy A. Rowan of Blue Hill has been elected assistant vice president of Fillmore County Bank here.

### Minnesota News

ALBERT LEA: The First National Bank has changed its name to First Northwestern National Bank, according to C. C. Bergerson, bank president. Northwestern has been added to more clearly identify the bank's 47 year affiliation with Northwest Bancorporation, bank holding company headquartered in Minneapolis.

BENSON: Tom Wiedenbush has been appointed vice president of The First State Bank. He most recently was vice president of the First National Bank at Miles City, Mont.

EVELETH: Robert P. Hatten has been elected president of the First National Bank. He most recently was assistant vice president in the commercial loan department of First National Bank of Duluth.

### Illinois News

The 85th annual convention of the Illinois Bankers Association will begin May 23 at Stouffer's Riverfront Towers in St. Louis, Mo. About 1,200 Illinois bankers are expected to attend. Complete coverage will be featured in an upcoming issue of the Northwestern Banker.

### North Dakota News

The annual convention of the North Dakota Bankers Association begins May 19 at the Holiday Inn, Bismarck. Presiding will be Gerry C. Anderson, president, The Bank of Tioga and president of the NDBA the past year. Complete convention coverage will be featured in the June issue of the Northwestern Banker.

ROLLA: Earl L. Loken has been elected president and managing officer of The First Bank. He formerly was vice president and cashier at The First State Bank of Cando.

### South Dakota News

TYNDALL: Security State Bank has increased its capital from \$100,000 to \$200,000.

### Wyoming News

GREEN RIVER: An application for a charter for a proposed South Side State Bank here has been filed in Cheyenne by five Casper men.

### BANKING SYSTEM . . . . . [Continued from page 1]

Examining the impressive penetration of banking into the credit

markets, the Salomon Brothers' partner pointed out that the ratio of new commercial bank funds to total funds supplied to the credit markets by all financial institutions averaged 27% from 1956 to 1960, 40% from 1961 to 1965, 45% from 1966 through 1970, and 49% from 1971 to 1974. But the ratio then fell to 22% last year.

### Roadblocks

Currently, he noted, there are formidable roadblocks in the way of banks further enlarging their share of the intermediation market. He stated:

• "Banks are experiencing considerable difficulties in pricing loans at competitively attractive interest rates. Bank lending rates currently exceed commercial paper rates by 1.75 percentage points. The result is that larger, better-rated corporations will finance more of their working capital requirements in the commercial paper market;

• Commercial banks' investment policies are conservative rather than aggressive. The need for tax-exempt income has declined, resulting in a sharp contraction in purchasing municipal securities. Their huge purchases of U.S. Treasury securities have been in the short-term area, reflecting an unwillingness to take significant money market rises.

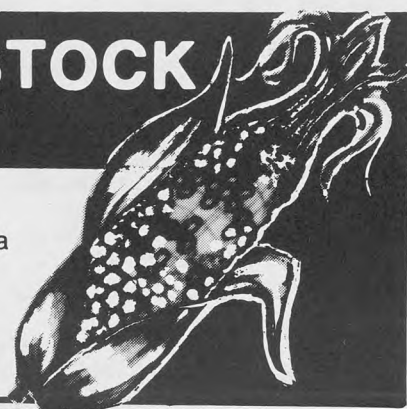
• Internationally, the banks are not likely to return to the hectic lending pace of a few years ago. Credit risks in foreign lands have increased, debt structures are top-heavy and inflation remains high. In addition, the rapid growth of

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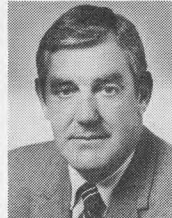
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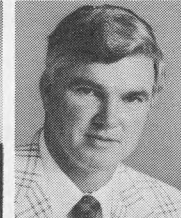
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American multi-national corporations, which U.S. banks helped finance, is over for the time being."

Mr. Kaufman pointed out, in reviewing the financial excesses of recent years and corrections now taking place, that "what is conducive can be harsh and what is harsh can be conducive." Conditions in the early 70s, he said, which were regarded as conducive to rapid banking expansion, have had harsh results. But, the new realism and weeding out of past banking excesses can be conducive to future orderly growth.

The experience of the past decade, he said, "is likely to have a profound impact on bank management, including the pricing of services and the scope of banking activities."

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